

TRANSPARENCY AND THE FINANCIAL STRUCTURE OF THE INTERNATIONAL MONETARY FUND

HEARING

before the

**JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES**

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

July 21, 1999

Printed for the use of the Joint Economic Committee



U.S. GOVERNMENT PRINTING OFFICE

WASHINGTON: 1999

cc 59-997

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, D.C. 20402

JOINT ECONOMIC COMMITTEE

[Created pursuant to Sec. 5(a) of Public Law 304, 79th Congress]

SENATE

CONNIE MACK, Florida, *Chairman*
WILLIAM V. ROTH, JR., Delaware
ROBERT F. BENNETT, Utah
ROD GRAMS, Minnesota
SAM BROWNBACK, Kansas
JEFF SESSIONS, Alabama
CHARLES S. ROBB, Virginia
PAUL S. SARBANES, Maryland
EDWARD M. KENNEDY, Massachusetts
JEFF BINGAMAN, New Mexico

SHELLEY S. HYMES, *Executive Director*
JAMES D. GWARTNEY, *Chief Economist*
HOWARD ROSEN, *Minority Staff Director*

HOUSE OF REPRESENTATIVES

JIM SAXTON, New Jersey, *Vice Chairman*
MARK SANFORD, South Carolina
JOHN DOOLITTLE, California
TOM CAMPBELL, California
JOSEPH R. PITTS, Pennsylvania
PAUL RYAN, Wisconsin
PETE STARK, California
CAROLYN B. MALONEY, New York
DAVID MINGE, Minnesota
MELVIN L. WATT, North Carolina

CHRISTOPHER FRENZE, *Chief Economist to
the Vice Chairman*
ROBERT KELEHER, *Chief Macroeconomist to
the Vice Chairman*

CONTENTS

OPENING STATEMENT

Representative Jim Saxton, Vice Chairman	1
--	---

WITNESS

Statement of Harold J. Johnson, Jr., Associate Director, National Security and International Affairs Division, U.S. General Accounting Office: Accompanied by Gary T. Engel, Associate Director, Accounting and Information Management Division, Phyllis Anderson, Senior Evaluator, and Thomas Melito, Senior Assistant Director	2
---	---

SUBMISSIONS FOR THE RECORD

Prepared Statement of Representative Jim Saxton, Vice Chairman . .	31
Prepared Statement of Harold J. Johnson, Jr., Associate Director, National Security and International Affairs Division, U.S. General Accounting Office: Accompanied by Gary T. Engel, Associate Director, Accounting and Information Management Division, Phyllis Anderson, Senior Evaluator, and Thomas Melito, Senior Assistant Director	33
Answers to Representative Saxton's letter on the IMF	
Follow-up to testimony, General Accounting Office Report, "International Monetary Fund: Observations on the IMF' Financial Conditions," September 1999	

TRANSPARENCY AND THE FINANCIAL STRUCTURE OF THE INTERNATIONAL MONETARY FUND

Wednesday, July 21, 1999

**CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
WASHINGTON, D.C.**

The Committee met pursuant to notice, at 10 a.m., in Room 311, Cannon House Office Building, the Honorable Jim Saxton, Vice Chairman of the Committee, presiding.

Present: Representatives Saxton, Sanford, Ryan, and Watt.

Staff Present: Christopher Frenze, Bob Keleher, Colleen Healy, Darryl Evans, Howard Rosen and Daphne Clones.

OPENING STATEMENT OF REPRESENTATIVE JIM SAXTON, VICE CHAIRMAN

Representative Saxton. Good morning.

It is a pleasure to welcome Mr. Johnson and his colleagues from the General Accounting Office (GAO) here before the Joint Economic Committee (JEC) once again. GAO testimony has been an important part of the JEC's program to provide more transparency to the financial structure of the International Monetary Fund (IMF). We very much appreciate their assistance.

The ongoing JEC review of IMF finances in recent years has involved much effort in seeking more transparency for IMF operations. I would like to thank Mr. Johnson and his GAO team for their hard work in helping the Congress to gain access to IMF information that for too long has neither been publicly available nor easily understandable.

I would like to just ask unanimous consent that my entire statement be placed in the record. In the interests of time, we will move right to Mr. Johnson's statement.

Sir, you may begin. Thank you very much for the great effort that you have put into this undertaking. We appreciate it very much, and we are anxious to hear from you.

[The prepared statement of Mr. Saxton appears in the Submissions for the Record.]

**STATEMENT OF HAROLD J. JOHNSON, JR., ASSOCIATE
DIRECTOR, NATIONAL SECURITY AND INTERNATIONAL
AFFAIRS DIVISION, U.S. GENERAL ACCOUNTING OFFICE:
ACCOMPANIED BY GARY T. ENGEL, ASSOCIATE DIRECTOR,
ACCOUNTING AND INFORMATION MANAGEMENT DIVISION,
PHYLLIS ANDERSON, SENIOR EVALUATOR, AND THOMAS MELITO,
SENIOR ASSISTANT DIRECTOR**

Mr. Johnson. Thank you very much for your comments.

Before I begin, I would like to introduce my colleagues.

To my immediate left is Gary Engel, who is an Associate Director with our Accounting and Information Management Division. He is jointly responsible with me for the overall work that we are doing in this area at the IMF.

To my right, immediate right, is Phyllis Anderson, a Senior Accountant, and Tom Melito, a Senior Economist, who have day-to-day responsibility for the work that we perform. I think most of our team wanted to participate in this hearing today, and they are behind me.

Before I begin my statement, you mentioned about the transparency that is gradually evolving at the IMF. I don't directly cover that in my statement, but I would like to comment that through the efforts of this Committee as well as others the IMF has become more transparent. They have some way to go yet, I believe, but they are making some progress in that area. They release a wide variety of information now with regard to their consultative process with countries as well as financial information. So I think you are making some headway in that regard.

My remarks today are basically based on work that we have done for this Committee as well as work that we have under way to meet the mandate of the *Omnibus Appropriation Act of 1999*. Since that work is ongoing, some of the information that I will present will be based on our preliminary analysis. We expect to complete that work and report to the committees that are cited in the legislation by September of this—by the end of September.

As you requested, today I am going to talk about the Fund's current situation regarding quotas, that is, the resources that the IMF obtains from its members and that it uses for most of its financial operations. I am going to discuss the level of resources that the Fund has reported as actually being available to lend and other resources that the Fund

potentially has available for conducting its operations, such as resources obtained through borrowing and the Fund's gold holding.

Also, as you requested, I will provide some historical perspective highlighting the share of IMF financial resources that have been contributed by the G-10. Incidentally, the G-10 consists of 11 countries. When we get to the charts you will see 11 countries listed for the G-10.

Before I summarize my statement, I would just like to briefly go over some background information that I think places some of this in context and makes it more easily understood.

Quotas are the membership dues that countries pay to belong to the IMF and comprise the bulk of the Fund's resources. Up to 25 percent of the quotas are normally paid in reserve assets which are either special drawing rights (SDRs) or freely usable currencies. The balance may be paid either in the country's domestic currency or with noninterest-bearing promissory notes.

The portion paid in freely usable currency or in SDRs is referred to as the member's reserve tranche position. This can be drawn by the member as needed, and if withdrawn is to be replaced by the member's own currency. The members are not required to replenish the reserve tranche position.

When a member needs funds other than from its reserve tranche, IMF does not literally lend the money to the country. Rather, the country purchases the currency that it needs from the IMF with an equivalent amount of its own currency and then later repurchases its own currency using either SDRs or currency that is designated by the IMF. Because IMF's financial assistance is in the form of currency purchases, this transaction does not reduce the combined total of IMF's current holdings in terms of the SDR equivalents. Instead, the composition of the currency holding simply changes.

The IMF holds about 103 million ounces of gold, most of which it acquired prior to 1974 when its Articles of Agreement required that 25 percent of a member's quota subscription be paid in gold. The regular use of gold in IMF transactions ended in 1978 when its Articles of Agreement were amended to reflect the end of the fixed currency exchange rate system that had governed the international financial system up to that time.

The IMF values its gold at 35 SDRs per ounce. That is about, at the current exchange rate, about \$47 an ounce, which was its value at the time it was acquired by the IMF. Therefore, IMF's gold holdings are

valued on its balance sheet at about 3.6 billion SDRs or about \$5 billion. However, the IMF reports in a footnote to its financial statements the current market value of gold holding, which incidentally on July 14, I believe, was about \$26 billion. But, as you know, it has been fluctuating.

Now, I would like to summarize our main points.

On January 30 of 1998, the IMF Board of Governors approved a new quota level of 212 billion SDRs, which was a 45 percent increase from the prior quota of about 146 billion SDRs. The quota became effective in January of this year when members having 85 percent of the total quotas consented to the quota increase. As of April 30, which is the end of IMF's financial year, about five billion in quotas had not been paid to IMF by 27 members. Seven of those members are currently in protracted arrears and ineligible to consent or to pay their quotas until they become current on their obligations. In addition, there are 20 members who have not yet consented and have until the end of July this year to do so.

IMF quotas have grown substantially over the years. This growth has come from increased membership, eight general quota increases since 1959, and several special and ad hoc increases in quotas of individual members. General quota increases have ranged from about 34 percent to 61 percent.

The United States has historically contributed the largest amount of quota resources. However, the U.S. share of the quota has fallen from a high of about 39 percent of quotas, of total quotas, in 1945 to the current level of about 17.5 percent. The U.S. share has decreased primarily due to the expansion in membership over the years—152 new countries have joined since its founding. Nonetheless, the absolute size of the U.S. quota has increased, from about \$2.8 billion in 1945 to \$50 billion now. Those numbers are in nominal dollars. They are not inflated.

Figure one on page five of the prepared statement shows that growth. We have a graphic that shows how the growth has occurred over the years. Now, the dark columns represent inflation-adjusted dollars, or real dollars, and the white, (which is a little difficult to see) represent nominal dollars.

In July last year, we testified that about \$43 billion of IMF's resources were actually available at that time for lending or for other purposes. Today, I want to update that figure to April 30.

As before, the IMF begins with its total amount of resources. I am going to cite these in dollars so it is a little easier to visualize. Its total

resources are about \$287 billion as of April 30. IMF estimates that, before considering the credit that has already been extended, about \$195 billion, or 68 percent, is usable. This is shown in figure two of the prepared statement on page six.

The usable resources consist of (1) currencies of members considered by the Executive Board to have sufficiently strong balance of payments and reserve positions for their currencies to be used in IMF's operations and (2) IMF's holdings of SDRs. The remaining \$92 billion of resources is considered unusable. That would be the white wedge in the pie chart.

This unusable amount consists of currencies of members that are currently using IMF resources and are therefore in a weak balance-of-payment position; currencies of members in relatively weak external positions; gold holdings of the Fund which require an 85 percent vote by the Executive Board to be used; and other nonliquid assets such as buildings, facilities, and that type of thing.

Over the past 10 years, from 29 to 39 countries have had currencies sufficiently strong to be used in IMF's operations. These percentages are shown in figure 3 on page seven of the prepared statement.

About 77 percent of the resources IMF deems usable were contributions by the G-10. The United States is the single largest contributor of usable resources with about 26 percent of the total.

Thus, as I have indicated, as of April 30, 1999, IMF had \$195 billion of total usable resources to meet—first of all, requests for funds and, second, to meet possible requests by creditor members for their reserve assets. IMF takes several steps to calculate the available and uncommitted resources referred to as liquid resources. That is shown on table 1.

The IMF first reduces the total usable resources by the amount of outstanding credit extended, in this case about \$81 billion, to determine available resources. It then reduces its available and usable resources by \$18 billion for commitments that are already made to countries and by about \$19 billion for a minimum working balance reserve that IMF believes is necessary to make payments in specific currencies. The minimum working balance is set at 10 percent of the quotas of members in a strong external and reserve position. This is shown graphically in figure 4 on page eight of the statement.

Over the past 20 years, the amount of usable and unusable resources has varied. Usable resources over the period has averaged about 60

percent of the total resources, with a significant portion being from the G-10. This is shown in figure 5 on page nine of the prepared statement.

The United States has been the major contributor to these resources. The U.S. portion is represented by the very dark line at the bottom of the bar graph.

IMF can also borrow to conduct its operations but historically has done so only from official sources. The Fund has not borrowed from private capital markets, although the Articles of Agreement permit it to do so, because, according to the Fund, it is a cooperative governmental institution whose basic purpose is to facilitate the overall adjustment process using surpluses to assist countries in deficit positions.

IMF first activated its general arrangements to borrow credit lines in 1964, and during the 1970s financed from 45 to 62 percent of its credit through borrowing. Since 1985, IMF has decreased its borrowing substantially and between 1992 and 1997 did no borrowing.

IMF resumed borrowing in July 1998 when it borrowed \$2 billion through the General Arrangements to Borrow (GAB) process to finance assistance to Russia and again in December 1998 when it borrowed about \$4 billion through the New Arrangements to Borrow (NAB) for Brazil. Both of these amounts were repaid in March of this year after IMF received funds from its quota resources.

I will turn just briefly to the gold issue.

IMF stresses the importance of gold as a reserve asset for the Fund. In 1995, IMF's Executive Board reviewed the Fund's position on holdings of gold as a reserve asset and announced several principles for managing gold reserves. These principles are that, one, gold provides a fundamental strength of the IMF; two, gold provides operational maneuverability in the IMF's use of its resources and adds credibility to its precautionary balances; three, gold should be held to meet unforeseen contingencies; four, IMF has a responsibility to avoid disruption in the functioning of the gold market; five, profits from gold sales should be retained and only the income from such profits or investments of those profits should be used for agreed-upon purposes.

Over the years the IMF has sold gold for a variety of reasons. On several occasions it had to replenish its currencies in the early 1950s and 1960s and used gold to buy those currencies. Also, it sold gold to generate some income needed to offset some operational deficits. And then between April 1976 and May 1980 IMF sold 25 million ounces of gold at auction to finance an IMF trust fund which had been created to

support concessional lending to low income countries. Finally, between 1977 and 1980, the IMF restituted 25 million ounces in gold in four annual installments to members in proportion to their relative quota shares as of August 31, 1975. The United States received an acquisition of 5.74 million ounces of gold in that transaction.

There have been several recent proposals to sell gold. These are discussed at some length in our prepared statement. But in order to preserve more time for questions and answers, I will not discuss the current proposals. If you would like to ask questions about them, we are prepared to respond.

That concludes my prepared remarks, and we are ready to attempt to answer your questions.

[The prepared statement of Mr. Johnson appears in the Submissions for the Record.]

Representative Saxton. Mr. Johnson, first, let me thank you for a very clear and understandable statement.

Let me also say that you mentioned that the IMF has become somewhat more transparent. We would like to thank you and your team for the hard work that you have put into this undertaking because, without the hard work that you have done, the understanding that this Committee and the Congress has gained would not have been possible. We thank you for that.

Let me ask you some questions about several items that you have made reference to.

First, sometimes official sources state that the United States contributes about 18 percent, I think it was 17.5 percent in your statement, as that would be our percent of the IMF quotas. However, it is also true, is it not, that if one were to set aside contributions that are not usable or useless, isn't the United States' contribution 26 percent? I believe you said that in your statement.

Mr. Johnson. Yes, that is correct. Twenty-six percent of those resources that are usable within the operational budget. The countries that are in and out of the operational budget fluctuate from time to time but, basically, on the margin. There are generally a fixed number of countries that are part of the operational budget that primarily support the Fund.

Representative Saxton. As a matter of fact, figure 3 in your statement, which you also had up on the board, shows the United States'

contribution in terms of usable quota to be 26 percent. Then the next largest would be Germany at only 9 percent; is that correct?

Mr. Johnson. Yes, that is correct.

Representative Saxton. And the United Kingdom would be next with 7 percent. So it shows that by far and away the United States' usable contribution is several times that of the next contributor.

Mr. Johnson. Yes, that is correct.

Representative Saxton. Under IMF rules, 25 percent of the quotas are paid in usable resources. However, isn't it the case that some countries, such as the United States, contribute more than 25 percent of quota in usable resources while other countries maintain virtually no contribution in hard currency?

Mr. Johnson. Well, the way that the process works is that, when a quota or subscription is agreed to, all countries have to provide 25 percent in hard currency or in SDRs. However, countries that are in a weak financial position or are borrowers sometimes are able to obtain those hard currencies or SDRs through some other means, make their payment and draw those funds out again. That is reflected, I believe, on tables at the end of the statement that show those countries that are creditor, the ones that are in a neutral position and those that are in a debtor position. They have basically drawn all of those funds out.

Representative Saxton. Now, as we all know, there has just been a quota increase. Nonetheless, about 88 percent or nearly half of the IMF members have a reserve position of less than 5 percent of quota, with many of these below 1 percent of quota and some at actually zero. Apparently, many of these nations borrow their reserve contributions to satisfy membership requirements and immediately withdraw it and repay lenders, including the United States.

Is this the case and if so, wouldn't it be more straightforward to just waive the IMF contribution rules if they are just going to be evaded anyway? What is the point in maintaining rules that suggest broad-based financial support when this is really not the case?

Mr. Johnson. I think the latter part of your question really goes to a policy issue that needs to be taken up with the Treasury Department.

I think there are some valid reasons, again, on the margin for holding to the process that they go through so long as the decision is to finance the Fund through equities rather than through borrowings. But

it does provide a mechanism for showing the total amount of resources that the IMF is responsible for, whether they are usable or unusable.

But I think your question is a good one, and it is something that could be discussed with the Treasury Department.

Representative Saxton. I was struck when I looked at the tables at the end of your statement. The IMF, at one point at least, likened their structure to a credit union.

Mr. Johnson. Yes.

Representative Saxton. In other words, if you were a member of the credit union, one would assume that you had a cash position in the credit union. These tables, I believe tables 1, 2, and 3, show the United States, for example, reserve tranche position as a percentage of quota at 46 percent and a number of other countries, including the UK which is at 37 percent and Australia which is at 43 percent.

Then when you move on to table 2, there are a number of other countries that appear with less than 5 percent of reserve tranche position. And then about two-thirds of the way down on page one of table 2, we begin to see a whole number of countries that have no reserve tranche position represented by 0s.

Then when we move on to table 3, all of page two and—well, all of page three, I was going to say, but there are only two on page three—demonstrate quite clearly that there are some 80 or 90 countries that actually have no reserve tranche position.

Mr. Johnson. That is correct. Table 3 represents the borrowing countries that have already withdrawn their reserve tranche and have called on resources outside of their reserve tranche.

Representative Saxton. Mr. Johnson, of the total amount contributed in excess of 25 percent of member quota in usable resources, what percent is contributed by the U.S., Japan, Germany, and France combined?

Mr. Johnson. Do you have that number?

I believe all of the G-10 is 77 percent, but—yes. I don't think we had added up the percentage for those five countries that you mentioned, but they contributed about 75 percent.

Representative Saxton. So it is clear that the industrialized countries provide better than three quarters of the total assets.

Mr. Johnson. Yes. I think it has become—the institution and how it functions has evolved over the years. In recent years, there has become a much greater distinction between the providers of capital and the users of capital. Clearly, the industrial countries are the providers. They have not drawn even on their own reserve tranche for a number of years. I believe the last drawing was in 1988. So there has been an evolution in the way the Fund operates. That is fairly clear in looking at the numbers.

Representative Saxton. On another closely-related subject, what is the current rate of interest that the United States has paid on its IMF contribution?

Mr. Johnson. I am going to ask Gary—

Mr. Engel. The rate that who is paying? The United States?

Representative Saxton. Yes.

Mr. Engel. Well, basically, for the United States to lend the money to be used by the members, they have to borrow from the public. For 1998, those rates ranged from, if it is a short-term borrowing, which are Treasury bills, about 5 percent and to the mid-term, which are notes, 6 percent, and for the long-term securities, those were about 8.5 percent.

Representative Saxton. Are you saying that the IMF pays those interest rates?

Mr. Engel. No. Maybe I misunderstood. That is what it cost the United States to lend the money to be used.

Representative Saxton. Okay. That was my second question.

My first question was, what is the rate that the IMF pays the United States for our contribution?

Mr. Engel. The remuneration rate for 1998 was about 4 percent. I believe that was before burden-sharing adjustments.

Representative Saxton. So if the United States were to borrow the money which we would then contribute to the IMF, we would then pay, as you noted, anywhere from just under 6 percent to 8 percent; is that correct?

Mr. Engel. Yes. If the money that we borrowed was through long-term lending, it would be more in the 8 percent range. I think generally it is more in the 6 percent range. So it is about a 2 percent difference.

Representative Saxton. Then the IMF pays us an interest rate of about half that 8 percent?

Mr. Engel. Yes, 4 percent for 1998.

Representative Saxton. One could make the case that the United States' taxpayers are subsidizing the IMF with low interest rates; is that correct?

Mr. Engel. There is an interest difference, yes.

Representative Saxton. Regardless of rationale used by the IMF, the IMF interest rate paid to the Treasury is far below the rate—the Treasury cost of borrowed funds, is the point that I am trying to make; is that correct?

Mr. Engel. Yes.

Representative Saxton. The JEC has concluded that the United States' gold contribution as of 1996 amounted to about 1.675 billion SDRs. The IMF has a complicated formula one can use to come to this conclusion or one can just take 25 percent of the total 1975 U.S. quota. That would amount to \$2.2 billion, would it not?

Mr. Engel. Yes.

Ms. Anderson. Yes.

Representative Saxton. Thank you.

Let me just say here that it seems to be clear from the data that the United States is the single largest source of IMF funds by far. Not only is the IMF quota relatively high, but the United States consistently contributes a larger portion of its usable funds as well as a higher proportion of the excess reserve contributions that go far above the minimum contributions. These resources are provided to the IMF in return for an interest rate that is far below the Treasury's cost of funds, thereby demonstrating a significant subsidy at taxpayer expense. The size of this subsidy appears to amount to hundreds of million dollars annually. I think that that is something that everyone should understand.

Let me ask about remunerated reserve, the nonremunerated reserve position. The IMF's Treasury booklet talks at length about a position—a portion of the member's reserve position on which the member receives interest but doesn't directly address the portion of which interest is not paid. Is there a portion of our contribution that does not receive interest, a nonremunerated reserve position?

Ms. Anderson. Yes, there is.

Representative Saxton. Doesn't this equal about \$2.2 billion?

Ms. Anderson. That is correct.

Representative Saxton. Why doesn't the United States receive interest on this portion of the contribution?

Ms. Anderson. The \$2.2 billion represents in U.S. dollars what the initial gold reserve tranche contribution was to the IMF, the U.S.'s share in 1978. The IMF's policy is that since gold is a noninterest-bearing asset, meaning it doesn't make any money off its gold, then it believes that it should not pay its members for the initial amount of the gold that they contributed.

Representative Saxton. So the IMF position is that, inasmuch as we have \$2.2 billion worth of gold, it is their position not to pay interest on that value; is that correct?

Ms. Anderson. That is correct.

Representative Saxton. Isn't the IMF justification on this issue contradictory? On the one hand, the IMF would argue that the United States should not receive interest on this portion of its reserve because it reflects the gold portion, which cannot be used to generate interest according to IMF policy. But, on the other hand, the IMF turns around and argues that the gold belongs to the IMF.

If the gold tranche belongs to the IMF and not to the United States, then the United States' reserve position does not contain any gold and should be fully remunerated, should it not?

Mr. Johnson. One could make that argument.

The way that transaction worked when the amendments to the Articles of Agreement were passed in 1978 was that the gold, as you stated, stayed with the Fund, but SDRs were substituted in the accounts in place of the gold. Now, one could argue that the SDRs do earn interest and therefore should be paid. Again, those are policy issues that need to be taken up with the Executive Branch. We wouldn't necessarily have a position on that policy.

Representative Saxton. I understand. But isn't it true that the IMF position is that the gold tranche belongs to the IMF and not to the U.S.?

Mr. Johnson. That is correct, yes. At least that is the IMF's interpretation, and the Treasury Department has not disputed that. We have had that discussion with Treasury, and they essentially agree with that position.

Representative Saxton. Thank you.

Well, setting aside any IMF rationalizations for this treatment, what is the cumulative value of the lost interest payments on this \$2.2 billion

from 1975 to 1999? In other words, we have not received—whether we argue that the United States owns the gold or that the IMF owns the gold, we have not received any interest payments. What is the cumulative loss to U.S. taxpayers?

Ms. Anderson. We actually have the number as of 1980 through 1999. That number is about \$3 billion. So it would be a little over—about \$3.5 billion.

Representative Saxton. \$3.5 billion?

Ms. Anderson. Yes, of interest that we have not received because of the—our remunerated portion of the reserve tranche.

Representative Saxton. Let me just say here, in addition to the subsidy mentioned before, there is a portion of the U.S. reserve position totaling over \$2 billion in which the IMF pays no interest. The cumulative value of this subsidy at the expense of the taxpayers has been estimated, as you just said, in the billions. You estimate \$3.5 billion from 1980 to 1995, and of course the gold has been there since 1975.

Mr. Johnson. The gold essentially accumulated over a period of years prior to 1974 when the initial tranche was paid in gold. And there were some—it was a progression. It wasn't all paid in at one time but through that period of time.

Representative Saxton. Thank you.

I would like to just move onto one other set of issues involving gold. Under the gold restitution formula in the IMF articles, eventual restitution would return about 23 percent of the total gold sold under this provision to the U.S., would it not?

Mr. Johnson. That is correct, yes.

Representative Saxton. In your statement you say that the market value of gold is about \$26 billion as of this year. Although I do not favor any form of IMF gold sales in the foreseeable future, I would like to ask a question based on the market value cited in your statement. If 10 percent of the IMF gold were restituted, that is 10 million ounces, it would be worth about \$2.6 billion. Under the restitution formula this suggests that the United States' net gain would be about half a billion dollars; is that correct?

Mr. Johnson. I believe that is correct.

Do you have those numbers, Tom, for us?

Ms. Anderson. For 10 million ounces?

Representative Saxton. Yes.

Ms. Anderson. That is true, yes.

Representative Saxton. About \$500 million?

Ms. Anderson. Yes.

Representative Saxton. I think it is also valid to think of the implications of any precedent that could be construed as giving up potential U.S. gains on the gold over the long-run, especially since the United States' stakes are quite large. Viewed from the perspective of the restitution provisions, wouldn't the U.S. share of the IMF gold be viewed as \$4.7 billion net of purchase cost? In other words, does this figure seem about right to you? No one is advocating liquidating all of the IMF gold, but isn't it useful to consider the fact that the United States has a considerable stake in the potential outcome of different types of gold sales?

Mr. Johnson. Yes. I think that is the right number.

If the gold were restituted, of course, that would presume then that the gold would be sold at market, which does fluctuate from time to time, basically on a daily basis, right now. So the amount of profit would vary. But even if the gold were restituted to the members under the formula outlined in the Articles of Agreement, it doesn't necessarily mean that the governments that receive that gold, including our government, would make a decision to put that gold on the market.

Representative Saxton. In your statement you have included an illustration of the proposed distribution which is a very general type of illustration. Has the Administration or the IMF given you any clues about the specific components of their proposal?

Among the questions that arise are the following:

First, what is the proposed schedule of gold sales and what specific criteria is it based on?

Second, how much interest would be available in each of the first three years for debt restructuring?

Third, how does the amount of proceeds that the IMF would receive from the capital value of the gold sales compare with the total interest generated for debt restructuring in the first three years? It appears that, over this time span, the IMF could receive more from the gold sales than is generated from interest or for debt restructuring.

Fourth, when the securities generating the interest mature, exactly where will the proceeds go? Where will the IMF—will these proceeds actually end up?

Mr. Melito. The IMF board discussed this issue last week. It is a nonpublic paper, but some of it was in the press.

They are debating the modalities right now, which methods for selling the gold. The issues include using the central banks or going directly to the market themselves through auction. The interest charge they get from this, again, is not public, but the things they have discussed are basically purchases of sovereign debt instruments. I think they expect a 5 percent or so interest rate.

We don't have the analysis right now about what their projected income would be from this. That would be something that we want to look at closer.

They are projecting, I do know, a stream of revenues over a couple of decades. That is their notion, having the profits generate interest over an 18- or 20-year period. But I don't have available a public number of how much that would generate.

As far as what happens to the actual trust fund at the end of that 18-year period, we have only had a discussion with Treasury about that. Treasury's understanding is the current thinking—it is just that, thinking on it—would be for that money to go to the General Resources Account at the end of that period. I would expect that would have to be written into whatever rules they have, and I'm not sure that has been worked out yet.

Representative Saxton. Did you get any specific numbers either from the Administration or the IMF?

Mr. Melito. There is a nonpublic document which discusses some of these numbers, but we are not at liberty to discuss that at this point.

Representative Saxton. Did they give you any specifics at all?

Mr. Melito. There are specifics on what they think the stream of interest earnings would be over this 18-year period in that document. There is also a discussion of the benefits, the advantages and disadvantages of certain methods of disposing of the gold discussed in that paper as well.

Representative Saxton. Do you think those numbers should be disclosed to Congress?

Mr. Melito. That is up to the Administration and Treasury.

Representative Saxton. Mr. Johnson, Webster's dictionary defines the term "restitution" as follows: "a giving back to the rightful owner of something that has been lost or taken away; restoration." The term "restitution" is the IMF's own description of its procedure for return of gold to donor nations, not mine. If the IMF really believes all of the value of the gold belongs to the IMF, why would it adopt the term restitution for the return of gold to member nations? The IMF is noted for unclear and confusing terminology. Why would it choose such a clear, unambiguous term as "restitution" unless the actual situation is somewhat more ambiguous and complicated than they are maintaining?

Mr. Johnson. I am not actually sure where they came up with that terminology, but basically all that means is they are going to sell the gold back to the members that provided it in the first place and would sell it at a rate of 35 SDRs per ounce.

Representative Saxton. Let me suggest that the explanation that there wasn't a unified point of view on this issue when the IMF charter was amended in 1978 and the point of view that much of the gold value belonged to the member nations was reflected in the use of the term "restitution" and the procedure itself.

Mr. Johnson. There was a debate about that. That is correct.

Representative Saxton. Let me just say at this point—and then we are going to turn to Mr. Watt for whatever questions or comments he may have—there is a strong argument for considering the market value of gold in excess of the official price, which is equal to \$47 per ounce, to be the property of the original donor countries.

Regardless of the legal issue, however, it is clear that the use of the IMF restitution formula would return about 23 percent of the gold to the United States with the United States netting about \$180 million for every billion dollars in total gold sales through restitution.

This approach also suggests that the United States' share of the IMF gold holdings amounts to about or at least \$4 billion. While I am not suggesting an IMF gold sale and think that gold should be held as a long lost reserve, it is useful to consider the implications of the restitution in analyzing potential United States' cost of benefits. If the gold sales are conducted in some other manner, then the United States would lose \$180 million per billion in sales of potential restitution. This precedent could convincingly jeopardize U.S. claims on \$4 billion in IMF gold holdings.

I want to thank Mr. Watt for his patience here. I am sorry that that took so long, but I wanted to wade through all of that to get it on the record. Sir, the floor is yours.

Representative Watt. Thank you, Mr. Chairman. I appreciate your allowing time for a few questions.

Mr. Johnson, I am going to talk some about the gold sale issue. That is on page 12 of your testimony, your printed testimony.

There is a section that indicates that the U.S. Congress must approve a U.S. Executive Director vote in favor of the Fund's sale of gold in certain circumstances, and then there is a footnote that suggests that those certain circumstances deal with cases in which 25 million ounces of gold are being sold. Then I think the proposal that is being discussed is to sell 10 million ounces; is that correct?

Mr. Johnson. That is correct. The reference in the footnote has to do with the sale that occurred from 1976 through 1980. And the requirement in the law is that the Congress must approve a vote by the Executive Director in favor of selling gold to set up a trust fund in addition to the amounts that were sold during that period of time.

Representative Watt. So it is not actually a 25 million ounce—

Mr. Johnson. No. That has taken place already. The current proposal is 10 million ounces of gold. That would require legislative action to authorize the Executive Director to vote in favor of that. And as you know—

Representative Watt. You are saying it would or would not?

Mr. Johnson. It would.

Representative Watt. So that was the question that I wanted to get to. Is it the IMF's position that it would require—or it is our position—

Mr. Johnson. It is our position that it would require, yes. Because it requires an 85 percent vote to authorize such a sale, the United States could block that sale if such an approval was not forthcoming.

Representative Watt. Okay. Now, what is it that triggers that congressional approval, the establishment of a separate trust fund?

Mr. Johnson. A bill would have to be introduced. I understand that a bill has been introduced in the House Banking Committee that would authorize the Executive Director to vote in favor of a sale. Of course, there are other bills that have—

Representative Watt. That is not my question. My question is, what is it that triggers that requirement about this particular sale? What is it that triggers compliance with that?

Mr. Melito. Most sales of gold require the 85 percent vote of approval. The reason it says “certain circumstances” is because Treasury pointed out to us in the review phase of this testimony that there are a couple of very technical forms of gold sale which are not on the table right now which may not require congressional approval. All of the kinds of gold sale which have been recently discussed would require—

Representative Watt. So that is not an issue then?

Mr. Melito. No.

Representative Watt. Let me move to the next question, then.

On page 13 of your testimony, Mr. Johnson, in the first or second full paragraph, I guess, you indicate that the G-7 has endorsed this proposed sale. Would you talk a little bit about the circumstances under which that endorsement came and in what form it came?

Mr. Johnson. Yes. I would like Tom Melito to discuss that. He has been following the issue of the HIPC proposal for some period of time.

Mr. Melito. As part of the G-7 communique from Cologne, they endorse an expansion of the HIPC debt relief initiative. In that communique they also talk about financing of this initiative in certain respects. They endorse gold sales as one mechanism to help finance the IMF's share of the expanded HIPC.

Representative Watt. How did that endorsement take place?

Mr. Melito. The board of the IMF is composed of the member countries. The G-7, as was pointed out earlier, represent a large voting share of the IMF board. That would be an important part of gathering the 85 percent approval.

Representative Watt. So except for the technicalities of getting congressional approval, this is a done deal, I take it?

Mr. Melito. It is still an open policy issue. It is the Administration that has approved it, not the Congress.

Representative Watt. But aside from that, the country, the Executive Branch is on record in support of this?

Mr. Melito. The Executive Branch working through the House Banking Committee has introduced legislation for this.

Representative Watt. Walk me through, if you would, how the sale would translate itself into debt relief.

Mr. Melito. The gold would be sold at market value one way or the other—

Representative Watt. You might want to make reference to the chart on page 13. I am having a little trouble here figuring out how this actually and ultimately translates into debt relief.

Mr. Melito. I will refer to this as the left column, middle column, and right column. In the middle column, the first box, the first part of the sale—there are a number of different ways of approaching that—we don't really have any analysis on how they do it, but assume the gold is sold. The gold would then produce—revenue from the gold sale. This revenue is then divided into several components. The capital value of the gold, which is basically the amount which the IMF carries on its balance sheet, would go to the General Resource Account. The General Resource Account would have its liquid resources increased by this amount of money.

Representative Watt. Can you put a dollar figure on that?

Mr. Melito. It is \$47 an ounce for 10 million ounces. It is about \$500 million for the 10 million ounce sale.

Representative Watt. So \$500 million goes to the left and—

Mr. Melito. Yes—so the balance sheet of the IMF would not be affected. It would be transferring gold into a liquid resource. The profits from the gold sale, which is everything except the \$47 an ounce and—

Representative Watt. The approximate dollar amount for that would be—

Mr. Melito. It depends on the market value of gold. Currently, at 260, we are talking about \$230 an ounce. So \$2.3 billion or so. It is a very variable market right now. You can't get very precise about it.

The profits would be placed in the ESAF HIPC trust fund. This amount of money in the ESAF HIPC trust fund would then be invested.

As I mentioned earlier, we are not sure exactly what investment instruments they are discussing, but in general the kinds of things they talk about would be sovereign debt instruments which earn around five percent interest rates, maybe some higher and some lower. It is the income generated from those investments which would be basically used to fund the HIPC as well as funding the shortfall in the ESAF. These are the two purposes for that fund.

Representative Watt. Has there been any discussion about exactly what countries would benefit from the debt relief? I mean, what form would that debt relief take?

Mr. Melito. The HIPC initiative is a multi-lateral and bilateral effort. The rules of the initiative use income levels of countries and their debt burdens as measured against certain statistics like export levels. Currently, about 41 countries are potentially eligible for HIPC. Under the Cologne initiative, they have projected about 33 countries would receive debt relief. For these 33 countries, debt relief is expected to be about \$27.4 billion. Out of that \$27.4 billion, IMF's share is \$2.3 billion.

The way that they provide debt relief varies by creditor. Some creditors will actually just remove the debt burden on the day that the debt is forgiven. Other creditors will pay off debt service as it comes due. Other creditors may give new debt at lower interest rates, a refinancing of it. It is really up to the creditor to decide how to provide the debt relief.

Mr. Johnson. I think it should be noted that in the case of IMF they do not forgive debt. So their process would be to help with the servicing of the debt rather than actual outright forgiveness.

Mr. Melito. That is correct. The IMF's likely approach to debt relief would be to pay debt service as it comes due. Over the 10 years of an ESAF loan, as the debt payments come due, IMF's likely approach would be to pay the debt service, as it comes using resources in the ESAF HIPC trust fund.

Representative Watt. If I follow through on everything you have told me—and correct me if I am wrong—you have about \$260 billion—what is it, 260—

Mr. Melito. \$2.6 billion from 10 million ounces? Yes. At \$260 an ounce, 10 million ounces would be roughly \$2.6 billion, and about \$500 billion of that goes to the General Resource Account. So approximately \$2.1 billion would be the profits from the gold sales. But the profits from the gold sales are not what actually is going to fund debt relief. It is interest on those profits.

Representative Watt. I think that is what I am getting to. In the final analysis, the bottom line that actually goes to debt relief is the interest from that part which turns out to be what amount?

Mr. Melito. That number is actually not available publicly at this point.

I would like to add, though, that the gold sale is not the only method of funding IMF's portion. In the Cologne initiative they discussed other methods, which include direct bilateral contributions. They talked about using the special contingency account which was created after the Latin debt crisis but no longer has a purpose. They also mention the possibility of using what are considered premium interest rates, which is the interest rates coming from the SRF (Supplemental Reserve Facility), the facility they used to support Brazil and Russia and Korea recently to help fund the HIPC.

Representative Watt. Do I understand this would trigger—this part of IMF involvement would trigger other debt relief?

Mr. Melito. The HIPC initiative is a joint effort by all creditors. So they all agree to a level of debt relief for a particular country. They then have to fund their own share of it. Once they target the amount of relief for a country, then it is an exercise, by going through the actual debt of the country to figure out what each creditor's share of the debt relief is.

Representative Watt. Did I hear correctly that that would be in a ratio of about 10 to 1?

Mr. Melito. The 10 to 1 you are referring to is how the U.S. scores its own debt relief to very poor countries. The U.S. has about \$6 billion worth of debt to the HIPC countries. Secretary Geithner in a hearing two or three weeks ago—

Representative Watt. I thought I heard the figures in the final analysis, you got to the bottom line, you got to 27.4 versus 2.3.

Mr. Melito. That is—the IMF's share of the 27.4 billion is 2.3 billion.

Representative Watt. So it would be about 10 to 1.

Mr. Melito. A little less than 10 percent.

Representative Watt. Thank you, Mr. Chairman. I just wanted to get a better understanding of this.

I understand the Chairman's position is that this shouldn't be done at all. I know it is a controversial issue, but it helps to understand what the impact is in the final analysis.

I yield back.

Representative Saxton. Thank you for your very thoughtful questions.

Let me just emphasize here that the one question that Mr. Watt brought up that I think is very interesting to which Mr. Melito said the figure is not available, if a little better than \$2 billion were invested and if a reasonable person said that it should have a reasonable rate of return of, say, 6 percent, that would translate into about \$120 million a year return on that investment. And so the gold sales with its advantages and disadvantages ends up throwing off about \$120 million for debt relief, which may or may not be considered a lot of money, particularly in light of the fact that it might be compared to the \$500 million that IMF is permitted under their proposal to keep for their own purposes. So the figure may not be officially available, but I think reasonable people could conclude that a little over \$100 million, \$120 million would be about right.

Mr. Johnson. It seems like a reasonable calculation, right.

Representative Saxton. Thank you.

Mr. Ryan.

Representative Ryan. Thank you. Thank you for coming today. I wanted to go down the same road that my colleague, Mr. Watt, went down. I would like to ask you about—Congress does have to approve the gold sale; is that not correct?

Mr. Johnson. The Congress must approve the Executive Director's vote in favor. So, in essence, that is correct.

Representative Ryan. Under the restitution charter, the sale, the IMF would have to pay 23 percent of the sale to the U.S.; is that correct?

Mr. Johnson. No. If restitution occurred, that would encompass the entire amount of whatever gold was offered.

There are different ways to conduct the sale of gold. One would be restitution, which is essentially a sale to the member countries. If gold were sold under the proposal that the Administration has made, then the proceeds of that sale would be allocated according to the method that Mr. Melito discussed. There would be no restitution under that process.

Representative Ryan. So if the Administration was proposing to do it under restitution by selling it back to the member countries, then the 23 percent rule would kick in?

Mr. Johnson. That would be the formula.

Representative Ryan. The United States would collect about \$180 million per billion of sales?

Ms. Anderson. Yes. If the restitution of the whole 24 million ounces were made, we would get—about \$5.1 billion would be returned to us in gold.

Representative Ryan. So under the current proposal for gold sales we would receive what, about \$470 million from restitution? What would that number be?

Mr. Melito. The current plan has no restitution component.

Representative Ryan. I know. But looking at the numbers—

Mr. Melito. Under 10 million ounces, it would be approximately 2.4 million of those ounces. If you would retribute, 10 million ounces would be for the U.S. My colleague will give you the dollar value right now.

Representative Ryan. I am glad somebody brought a calculator.

Ms. Anderson. It would be about the \$5 billion that was mentioned earlier.

Representative Ryan. Okay. So under restitution, which I know the Administration is not proposing restitution, that would mean that the U.S. would have to collect about half a billion dollars under this sale if they wanted restitution. This is something that I think—most Members of Congress don't have any idea how this works. It is a very complicated issue. If the IMF were going down the restitution road, that would be something where the U.S. taxpayer would be owed about half a billion dollars under this current proposal?

Mr. Johnson. For the 10 million ounces, correct.

Representative Ryan. That is something very important and worth noting, that the route that the Administration has chosen is to sidetrack the restitution route, which means the IMF would not have to pay the U.S. taxpayer \$500 million approximately; is that correct?

Mr. Johnson. It is correct. I don't know that I would characterize it quite like that. They have decided that gold is a way to raise money for the debt relief program that has been adopted. Gold would be one source of revenue for that.

Representative Ryan. So the sale would take place on the open market, correct?

Mr. Johnson. Well, I don't think they have gotten to the point of deciding how the sale would occur. In fact, I don't believe that that decision would be made until the fall general meeting in September. But

they have discussed four or five different modalities of sale. Auction on the open market would be one. A direct arrangement with central banks could be another. Using a bullion bank to conduct the sale would be another. There are various modalities that have been discussed, but they have only gotten to the discussion stage. There have been no decisions made that I am aware of on that.

Representative Ryan. Ms. Anderson, did you want to make a comment?

Ms. Anderson. I just wanted to say that if gold were restituted back to the United States, the United States would get gold back.

Representative Ryan. But that is not a modality that is being considered right now by the Administration. So the cost of that decision of not considering modality is roughly—I think it was about \$500 million—

Mr. Melito. Let me clarify that. If gold is restituted to the United States, the U.S. Government would owe the IMF about \$500 million. The U.S. have to pay the IMF at the official rate of gold. We would be receiving gold worth the market value, so—

Representative Ryan. Because of the difference between the 47, right.

Mr. Johnson. And, again, the profit would assume the sale of gold by the United States after it receives it. But in terms of value, you are correct.

Representative Ryan. I think that is a very interesting point because most members don't know what is at stake here.

Going down the road of the chart that Melvin brought out, under the ESAF agreement, how would you characterize the way ESAF would change if this plan is to go through? Would this be a case where there would be more of a permanent funding mechanism after they get the proceeds of the gold sale into the special disbursement account and is this something that, if we are kind of agreeing on the back of the envelope, that this is going to reap about \$120 million a year on something like a 6 percent rate of return? Would this not provide more of a permanent funding mechanism for ESAF?

Mr. Johnson. I believe that is correct. I would like Tom to talk about that a little more. He has done some preliminary calculations on that issue that I think would be helpful.

Mr. Melito. The trust fund that the IMF is setting up has two purposes. I am not sure this is actually well known. Its first purpose is to fund the IMF's share of HIPC. As I mentioned earlier, about \$2.3 billion as projected based on the Cologne initiative. The other goal is to fund the shortfall in ESAF, which is projected to start sometime in the early part of the next decade, in about five years.

We have a preliminary breakdown that separates these costs. There is \$2.3 billion for the HIPC. We think, working on IMF documents that are on their web page, that the ESAF shortfall is around \$2.7 billion, but that is very preliminary. That results in a total of \$5 billion for the two purposes. We know that they are mentioning several different ways of paying for that. Gold sales is one of the ways that we mentioned. They have several other purposes. So they are mixing two goals with several financing mechanisms.

Representative Ryan. Because you don't have all of the numbers, but the practical result at the end of the day is they would have more of a self-financing mechanism in place?

Mr. Melito. That is the goal, to have ESAF be self-financed. ESAF would be self-financed, even without getting this money, sometime at the end of the next decade. There is a temporary shortfall in ESAF that is being projected.

Representative Ryan. What—would this affect Congress in its role in oversight of these two funds?

Mr. Melito. That is a good question. That is not something which we have looked at, but clearly it becomes an issue under the current arrangement they have to periodically go to Congress for funding in one way or another such as the sale of gold.

Representative Ryan. We would have to do that then once—

Mr. Melito. That could be a potential implication. Again, we have not done analysis on that.

Representative Ryan. I am a member of the Banking Committee as well as the Joint Economic Committee, which I thank the Chairman for allowing me to sit on the Committee. That is the conclusion that many us in the Banking Committee have made, is that under this proposal this is one way, for a good reason or bad reason, to sidestep annual congressional oversight or review or approval of these funds.

I would just like to let my colleagues know that yesterday I sent a letter to Chairman Leach on the Banking Committee signed by 13 of my

Banking Committee colleagues opposing IMF gold sales. In the letter—I will just read a quick quote here. "We urge the Chairman to join us in ensuring that no provision for this gold sale is included in either the FY 2000 authorization request for the international financial institutions or in any other legislation pending before the Banking Committee."

This from a legislative track comes through in a few forms, under the authorization bill, under a debt relief bill. But many members of the Banking Committee, and this is just from the majority side of the Banking Committee, are steadfastly opposed to voting and approving this gold sale in the Committee. Under these very reasons, we don't know the specific modality. It is very clear that under either modality that they chose that we would lose oversight over the IMF, over IMF policies, over ESAF.

Mr. Johnson. That would be a possibility.

Representative Ryan. That is the possibility that seems to be of concern to many Members of the Committee. I think earlier we clearly discovered that there is a significant taxpayer subsidy that currently takes place because of the interest rate disparities with respect to the IMF. That is something that cannot be refuted, correct?

Mr. Johnson. Well, the taxpayer subsidy that you are referring to has to do with the General Resources Account more so than the ESAF. ESAF is very concessional.

Representative Ryan. Right. One of the things that we are concerned about in the Committee, and then I will go on to general IMF policy, is that fact that many Members of Congress have concern that while watching for the constituents dollars, making sure that taxpayer dollars are spent wisely, we are not doing good things. We are going down roads with IMF that many Members of Congress would not like to pursue, doing more harm than good in many of these cases.

Just to summarize, is it your opinion—and I just want to recap this real quickly—that on a restitution, \$180 million would have to be returned per billion dollar of sales? Now that the modalities they are considering are nonrestitution modalities, this would be a funding mechanism that would avoid restitution and it would be a funding mechanism that would put more permanent funding for the ESAF in the time being, thereby obviating any congressional oversight or approval in the meantime; is that correct?

Mr. Johnson. I would agree with that.

Representative Ryan. Thank you very much, appreciate it.

Representative Saxton. Thank you, Mr. Ryan.

Mr. Sanford.

Representative Sanford. I just have a couple of general questions.

I think that we have plowed through the ground very well on the issue of transparency and the financial structure of the IMF. Then I want to go from the microscope where we have been just to sort of the big picture. The big picture for me would be if you-all were to think of, let's say, the safest IMF investment, if you want to call it that, what would that be?

Mr. Johnson. I am sorry—

Representative Sanford. In terms of countries, what would be the safest IMF investment?

Mr. Johnson. I think there are probably some risks involved anytime the IMF provides funds for a country that is in crisis. It seems like the Asian countries are coming back so those funds will be returned.

One thing that we have observed in our analysis is that there has been a much greater concentration of funds going to fewer and fewer countries. For example, Russia has about 21 percent, I believe, now of the IMF resources.

Representative Sanford. So would you reverse it and say that Russia would be the worst IMF investment?

Mr. Johnson. Well, the riskiest.

Representative Sanford. I am saying, in terms of creditworthiness, if you had just a pendulum, just the back of the envelope kind of way, you would say that Russia might be toward the less creditworthy end of the scale and some country—this Southeast Asia might be on the upper end of the scale?

Mr. Johnson. That would seem roughly reasonable. It should be noted that when IMF makes its decisions it attempts at least to treat all countries the same and does not do a credit risk analysis.

Representative Sanford. I understand that. But in other words, given the cost of capital to these countries with the exception of a small category, broadly the rate setting is within a relatively narrow band, correct?

Mr. Johnson. Essentially the same.

Representative Sanford. Right. So what I am getting at is, given one country may be over here on the creditworthiness scale and the other country may be over here, there is no adjustment to the cost of capital, to wait and see what private markets. What I am struggling with is, therefore, is the IMF indirectly subsidizing bad policy?

Mr. Johnson. Well, the latter part of your question, I am not in a position to answer.

Representative Sanford. Again, you understand the point that I am making. If you were Lloyds of London there would be a direct credit risk premium..

Mr. Johnson. That is correct.

Representative Sanford. And therefore, since there isn't in this arrangement, in an indirect way, since we make it easier for capital to flow to a place that may have basket case policy, in other words, does it indirectly subsidize the continuation of bad policy?

Mr. Johnson. That may be one way to view it. The other way to view it is that the IMF places some fairly stringent conditions on countries to help them with their macro-economic situation, whatever that may be. And—

Representative Sanford. So in other words you would characterize it, in essence, as an aid program?

Mr. Johnson. Well, it is a program to help countries restructure their macro-economic policies so that they recover from the situation that they find themselves in.

Representative Sanford. Right. I went to credit school up in New York, the Chemical Bank training school, when I was straight out of college. I remember the 5 Cs of credit. What you are saying is basically IMF does not apply the 5 Cs. Rather than adjust in terms of premium based on the riskiness of that given investment, there isn't that adjustment. So one could legitimately make the argument that the IMF subsidizes bad policy, or, in reverse, we are not subsidizing but are an aid program to help those countries.

Mr. Johnson. The IMF is trying to correct that bad policy.

Representative Sanford. I guess the only other thought that I would have would be do you think that this aid program or these costs to the taxpayers ought to be built into the budget? Again, which is outside of your direct role, but in terms of the way we account for our budgeting

here in Washington to the United States taxpayer, do you think it ought to be built in?

Mr. Johnson. I am going to ask Gary Engel to respond to that. He is more familiar with the budget.

Mr. Engel. Right now, there is nothing, to my knowledge, built-in to the budget for a subsidy or even for an anticipated default. Under other programs such as credit reform, there is an up-front estimated subsidy, built-in to the cost so that you know what it is costing you to do the program..

Representative Sanford. You think that would be good or do you think that would be bad?

Mr. Engel. I think it would help decision-makers understand what it is really costing to participate in that program.

Representative Sanford. So if you had to pick, your vote would be yes, it ought to be an on-budget item so the taxpayer could see what it cost?

Mr. Engel. Well, as I understand it, it flows through the budget but it is not up front. I personally would be in favor of clearly knowing early on what it is estimated that it is going to cost. Right now what happens is the interest costs are part of a line item in the budget called interest on the Federal debt. So we don't really have an indication of what this difference in interest that we spoke of earlier in the hearing is costing us.

Representative Sanford. I sure appreciate your time. Thank you.

Representative Saxton. Thank you very much, and we appreciate very much again the contribution that you have made here.

Let me just conclude the hearing by saying that certainly, as representatives of the American taxpayers, we have here the obligation to point out several facts that you have been very helpful with. First, that the United States is the single largest source of IMF funds by far, and that the taxpayers of this country are contributors to that. And that these resources that are provided to the IMF in return for an interest rate, which is far below the Treasury's cost of funds, thereby demonstrates further a cost in addition to what we may contributing directly. And that, thirdly, in addition to the subsidy that I just mentioned, there is a portion of the United States reserve position totaling over \$2 billion on which the IMF pays no interest whatsoever, accounting for another taxpayer subsidy, if you will. And that, finally, what we are considering in the current

context is the sale of a portion of the IMF total gold holdings to which the United States share amounts to almost \$5 billion.

And so these are all matters which are of interest to us and of concern to us because of our obligation to the American taxpayer.

We thank you very much for the contribution that you have made. It has been a very important one, and we look toward to working with you as we proceed through these and other issues.

Thank you very much. The hearing is adjourned.

[Whereupon, at 11:23 a.m., the Committee was adjourned.]

SUBMISSIONS FOR THE RECORD

PREPARED STATEMENT OF REPRESENTATIVE JIM SAXTON, VICE CHAIRMAN

It is a pleasure to welcome Mr. Johnson and his colleagues from the General Accounting Office (GAO) before the Joint Economic Committee (JEC) once again. GAO testimony has been an important part of the JEC's program to provide more transparency to the financial structure of the International Monetary Fund (IMF), and we very much appreciate your assistance.

Transparency in IMF finances is needed simply because the IMF is a publicly funded institution in which the U.S. assumes a major financing and policy role. However, IMF financial activities are cloaked in an obscure accounting system designed in an era when the nature of IMF activities was very different from what it is today. Even the public financial statements of the IMF are confusing, as reflected in the inaccurate statements of a member of the IMF executive board before Congress last summer. While confusion about the IMF's public financial statements is quite understandable given their format, another problem is that the operational budget of the IMF is treated as a classified document.

The ongoing JEC review of IMF finances in recent years has involved much effort in seeking more transparency in IMF operations. Unfortunately, our review of IMF operations and promotion of IMF transparency has been hampered by IMF and Treasury refusals to publicly release documents such as the IMF operational budget and policy reviews that would permit consultation with independent experts. It became evident that if significant IMF financial transparency were going to occur, it would have to be directly provided through Congress. This was one factor leading to my request last year for assistance from the GAO in gaining access to IMF financial information.

By forcing additional financial information into the public domain, it was my hope that the activities of the JEC and GAO would result in more transparency and also reduce IMF incentives to withhold information related to that already in the public domain. In one of a series of JEC hearings last year, the GAO presented the first intelligible and reasonably complete overview of IMF finances available up to that time. Subsequently, the IMF has moved to make more of its financial information public, but this institution has a long way to go before it can be considered reasonably transparent. However, progress on other fronts

is being made. A recent positive development is the publication of a study on IMF finances by the Bretton Woods Committee which corroborates the conclusions of JEC research in this area in several key respects.

This hearing will focus on information related to costs of U.S. participation in the IMF as reflected in quotas, IMF interest payments to the U.S., potential gold sales and restitution, and budgetary treatment. Although it has not been easy, we now have the necessary analytical tools for uncovering the most relevant financial data so that independent appraisal and analysis of IMF operations can be facilitated. It is important that this information be made publicly available for informed policy analysis regardless of where we stand on the many policy issues related to the IMF. The GAO is making a presentation of factual material, and has not been asked to take a position on any issue currently before the Congress.

An assessment of the costs associated with United States' participation in the IMF suggests that the U.S. bears a disproportionate share of the costs of IMF operations. Further, these costs are often hidden or obscured by various accounting and other means. A review of IMF quotas indicates that the best measure of the U.S. share of IMF contributions is 26 percent, not the 18 percent figure officially circulated. However, it appears that the IMF does not pay the U.S. interest on over \$2 billion of its contributions, and the cumulative cost of this to the U.S. in recent decades has been significant. Another cost issue relates to proposed gold sales, which could impose direct costs to the U.S. and also affect a legitimate U.S. claim to several billions of dollars in gold assets. Finally, there is the question of whether the current budgetary treatment of the IMF fully complies with the recommendations in the Report of the President's Commission on Budget Concepts.

I would like to thank Mr. Johnson and the GAO team for all their hard work in helping the Congress gain access to IMF information that for too long has neither been publicly available nor easily understandable.